No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA AND RAYMOND J. LUCIA COMPANIES, INC.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR EQUITY DEALERS OF AMERICA AS *AMICUS CURIAE* SUPPORTING PETITIONERS

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INTEREST OF *AMICUS CURIAE*[1]

Equity Dealers of America (EDA) is a trade association that represents the retail and institutional equity capital markets interests of its financial services firm members. EDA members advise hardworking and retired Americans how to create and preserve wealth and provide Main Street businesses with access to capital and advisory services. The EDA believes fair, efficient, and competitively balanced equity capital markets are necessary to protect investors, advance financial independence, stimulate job creation, and increase prosperity. The EDA's mission is to promote public trust and confidence in the U.S. equity capital markets. The EDA advocates against one-size-fits-all, undifferentiated regulations that disproportionately impact middle-market financial services firms, small businesses, and retail investors.

The EDA works tirelessly with its members, regulators, and policymakers to promote financial inclusion, economic opportunity, and financial independence. In addition to policy advocacy and public outreach, the EDA hosts meetings on the equity markets to inform and educate its members on issues relevant to their businesses and to their clients. Professionals at EDA member firms actively engage in shaping and promoting the EDA's advocacy agenda by identifying regulatory and compliance concerns, and developing issue-specific white papers intended to

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[1] All parties have consented to the filing of this brief by blanket consent or letter. No counsel for a party has authored this brief in whole or in part, and no person other than *amicus curiae*, its members, and its counsel has made monetary contribution to the preparation or submission of this brief.

directly benefit EDA member firms, their clients, and investors.

Because the EDA advocates for the interests of middle-market financial services professionals, the EDA has a direct and substantial interest in this case. EDA's members at times find themselves part of administrative proceedings before the Securities and Exchange Commission's (SEC) administrative law judges (ALJs). Thus, the EDA has a particular interest in ensuring that the SEC's administrative proceedings are fair and afford its members due process.

SUMMARY OF ARGUMENT

This Court should reverse the judgment of the United States Court of Appeals for the District of Columbia. SEC ALJs "exercise significant authority pursuant to the laws of the United States." *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976). SEC ALJs therefore are inferior officers of the United States who must be appointed consistent with the Appointments Clause of the U.S. Constitution. U.S. Const. art. § II, 2, cl. 2. Because SEC ALJs oversee proceedings in which quasi-criminal penalties may be levied, they must be constitutionally appointed. Proper appointment of SEC ALJs is necessary to safeguard the liberty of SEC respondents in SEC proceedings. Yet, SEC ALJs are not appointed by the President, a court of law, or the head of a department. This Court should find that their appointments are unconstitutional, and reverse the decision of the D.C. Circuit. The appointment of SEC ALJs pursuant to the Appointments Clause is a critical first step in ensuring constitutionally adequate SEC proceedings.

The story of the SEC is the story of a regulatory agency that has slowly but steadily expanded its reach and its nearly unfettered ability to interpret and enforce the nation's securities laws. Throughout its existence, the SEC's powers have been expanded to allow the agency to enforce securities laws not only against regulated companies, but also against unregulated companies and individuals as well. As the SEC's mandate has grown, it has increasingly brought such enforcement actions in administrative proceedings before its in-house ALJs rather than in an Article III court.

When the SEC was created in the 1930s, "its enforcement powers were largely limited to seeking injunctions in federal district courts to enjoin violations of the securities laws, and the only express provision for administrative hearings was to suspend or expel member or officers of national securities exchanges." Jed S. Rakoff, PLI Securities Regulation Keynote Address: Is the SEC Becoming a Law Unto Itself? 3 (Nov. 5, 2014). As the SEC's powers expanded over the course of its existence, its ability to use administrative proceedings to enforce its mandate—including by seeking injunctions and civil monetary penalties—was limited to regulated entities. Pub. L. No. 101-429, 104 Stat. 931 (1990). If the SEC wanted to seek monetary penalties against unregulated entities, it had to proceed in federal court. See, *e.g.*, *Gupta* v. *SEC*, 796 F. Supp. 2d 503, 507 (S.D.N.Y. 2011).

In 2010, however, Congress passed the Dodd-Frank Act, which authorizes the SEC to seek monetary penalties through its administrative proceedings against *any* individual for a violation of

the securities laws. SEC ALJs now routinely handle matters that previously were the exclusive province of federal district court judges. See 15 U.S.C. 78d-1(a) (authorizing the SEC to delegate any of the Commission's functions to ALJs); 17 C.F.R. 200.14 (assigning ALJs responsibility "for the fair and orderly conduct of" SEC enforcement proceedings).

This expansion of SEC power has eroded the due process rights of SEC respondents who find themselves in the crosshairs of the SEC's Division of Enforcement (Division). SEC respondents—including *unregulated* entities and individuals—frequently are forced to defend themselves in administrative proceedings with fewer procedural safeguards than in Article III courts. When individual SEC respondents must face prosecution by an SEC attorney, in the SEC's forum, before an SEC ALJ, and without the constitutional procedural protections afforded in federal court, unsurprisingly, the SEC respondents rarely prevail.

The paucity of substantive and procedural safeguards of due process in SEC enforcement proceedings is particularly troublesome because ALJs are not even constitutionally appointed. Even this minimal due process check is left wanting. An agency with such far-reaching power and the ability to impose quasi-criminal penalties on "*any individual*" (registered and non-registered entities alike) must enforce laws and regulations through a constitutionally appointed actor. That is the purpose of the Appointments Clause. See *Buckley*, 424 U.S. at 126. The Appointments Clause "preserves * * * the Constitution's structural integrity" by ensuring that officials remain "accountable to political force and the

will of the people." See *Freytag* v. *Commissioner*, 501 U.S. 868, 878, 884 (1991). It is critical to the protection of SEC respondents' due process rights that ALJs be constitutionally appointed so that they can be held politically accountable for their conduct.

It was in this ill-constructed court that petitioners, like many other SEC respondents, found themselves in 2012, when the Division brought an action for violations of the Investment Advisors Act. The Division alleged that petitioners' client presentations on retirement wealth management strategy violated the Advisors Act. The ALJ found that the petitioners used misleading information when pitching their services to prospective clients, and imposed fines and a cease and desist order on petitioners. The ALJ further barred petitioner Raymond Lucia from associating with an investment advisor, broker, or dealer. See *In the Matter of Raymond J. Lucia Companies, Inc. & Raymond J. Lucia, Sr.*, Release No. 4190, 2015 WL 5172953 (Sept. 3, 2015).

The ALJ's decision violated the Constitution because the ALJ in this case, and all SEC ALJs, are without constitutional authority to issue decisions. As explained below, the SEC enforcement proceedings are constitutionally suspect under the best-case scenario—that is, with a constitutionally appointed ALJ. But that minimum protection is not even currently in place. Accordingly, to bring some measure of constitutional protection to SEC enforcement proceedings, the EDA respectfully requests that this court rule in favor of petitioners and hold that the SEC's ALJs are officers of the United States within the meaning of the Appointments Clause.

ARGUMENT

The constitutional appointment of SEC ALJs is critical to upholding the due process rights of individuals called before the SEC. SEC proceedings are "in some tension with Article III of the Constitution, the Due Process Clause of the Fifth Amendment, and the Seventh Amendment right to a jury trial in civil cases." *Lorenzo* v. *SEC*, 872 F.3d 578, 602 (D.C. Cir. 2017) (citing P. Hamburger, Is Administrative Law Unlawful? 227-57 (2014)). Multiple aspects of the SEC's administrative proceedings curb the due process rights of SEC respondents by tilting the outcome in the SEC's favor. SEC enforcement actions are not like civil actions between private parties—they are "quasi criminal proceedings" with the power to impose sanctions that "look[] like criminal penalties." See Tr. of Oral Argument at 34, *Gabelli* v. *SEC*, 568 U.S. 442 (2013) (No. 11-1274) (Breyer, J.); *Gabelli* v. *SEC*, 568 U.S. 442, 451 (2013) ("In a civil penalty action, the Government is not only a different kind of plaintiff, it seeks a different kind of relief."). Although an SEC proceeding may not explicitly be criminal in nature, it carries the same consequences as a criminal conviction—a sanction that imposes a lifetime bar from "the securities industry [is the] equivalent of capital punishment" to an individual's likelihood. *Saad* v. *SEC*, 718 F.3d 904, 905 (D.C. Cir. 2013).

Given the ramifications of such proceedings, an ALJ's status as a non-appointed adjudicator is troubling. Arguably, the very use of ALJs and Article I proceedings are unconstitutional. In the modern administrative state, federal agencies regularly exercise broad Article II legislative powers that have

been unconstitutionally delegated by Congress, and exercise Article III judicial power, usurping the constitutional prerogative of the federal courts. These violations of the doctrine of separation of powers threaten the liberty of every American. See *Morrison* v. *Olsen*, 487 U.S. 654, 693 (1988) ("[T]he system of separated powers and checks and balances established in the Constitution was regarded by the Framers as 'a self-executing safeguard against the encroachment or aggrandizement of one branch at the expense of the other.'" (citing *Buckley*, 424 U.S. at 122)). But separation of powers concerns are not the only ones. The premise that Article III review can somehow cleanse the unconstitutionality of Article I adjudication only doubles down on violations of separation of powers. "An agency's interpretation of a statute that it administers receives considerable deference under current law." See Gary Lawson, *The Rise and Rise of the Administrative State*, 107 Harv. L. Rev. 1231, 1247 (1994). "More fundamentally, agency *fact-finding* is generally subject to deferential review under numerous statutes that expressly require courts to affirm agency factual conclusions that are supported by 'substantial evidence.' This kind of deferential review arguably fails to satisfy Article III." *Ibid.*

Those constitutional concerns of Article I rulings are compounded by SEC enforcement that contains shortcomings in substantive and procedural safeguards. For example, the SEC's Rules of Practice limit the time in which enforcement cases must be tried to an initial decision, they restrict the ability of SEC respondents to conduct discovery, and they allow the admission of damaging hearsay evidence that would not be permitted in an Article III court. The

discovery limitations imposed on SEC respondents is especially worrisome, given that, upon review of a Commission determination in a federal court, the court is limited to the record created before the Commission. Where an SEC respondent has limited ability to create the record in the proceedings below, Article III review is ineffective. As a result of those shortcomings, the Division's preferred forum—administrative proceedings before SEC ALJs—deprives SEC respondents of procedural rights they would be afforded in Article III courts and infringes upon their due process rights.

Considering the Article I proceedings' shaky constitutional footing, it is even more important that the presiding ALJs are appointed in accordance with the Constitution.

I. The Procedural and Evidentiary Limitations Before ALJs in Administrative Hearings Deprive SEC Respondents of their Due Process Rights.

Proceedings before an SEC ALJ lack the procedural protections available to defendants in federal court. Those limits deprive the SEC respondents of their due process rights. The SEC imposes an accelerated schedule mandated by the Rules of Practice, places extreme limitations on discovery, and yet, at the same time, gives the SEC power to introduce evidence that would not be admissible in an Article III court.

Where companies and individuals must face quasi-criminal proceedings that carry potentially ruinous fines and a loss of a license that could mean

the loss of a livelihood, companies and individuals called before an SEC ALJ are entitled to the full procedural protections and due process rights afforded under the Constitution.

A. The Litigation Timeframe Required by the Rules of Practice Deprives SEC Respondents of their Due Process Rights

The SEC's accelerated adjudication process deprives SEC respondents of the time necessary to develop their defenses and gives the SEC Enforcement Division an unfair advantage. SEC administrative actions proceeding in compressed timeframe to an initial decision. 17 C.F.R. 201.360(a)(2). A hearing officer is required to file an initial decision with the Secretary of the Commission either 30, 75, or 120 days after (1) the completion of post-hearing briefing, (2) the completion of briefing on a dispositive motion pursuant to 17 C.F.R. 201.250 in the event the ALJ determines no hearing is necessary, or (3) the determination by the ALJ that a party is in default pursuant to 17 C.F.R. 201.155 and no hearing is necessary. 17 C.F.R. 201.360(a)(2)(i). The Commission has complete discretion to choose the 30-, 75-, or 120-day timeline "after consideration of the nature, complexity, and urgency of the subject matter, and with due regard for the public interest and the protection of investors." *Ibid.* The Commission thereby chooses whether the proceedings will be accelerated to be concluded within a single month or up to 10 months. *Ibid.*

This compressed timeframe jeopardizes SEC respondents' due process rights and places SEC respondents at an unfair disadvantage. The Division

has years to prepare its case, documents, and other papers, limited only by the five-year statute of limitation under 28 U.S.C. 2462. Indeed, the Division has, in the past, conducted a "dump" of a "massive file," which took respondents months to process. *Chau v. SEC*, 72 F. Supp. 3d 417, 426-427 (S.D.N.Y. 2014). The condensed schedule denies SEC respondents a meaningful opportunity to gather evidence from key witnesses or examine the extensive evidence that the Division has collected in often an extended investigation. The SEC respondents thus frequently lack time to develop an effective defense to an action.

In contrast, Article III courts have the power to set case management and trial deadlines that take into account the needs of both parties, the complexity of the case, and the protection of the due process rights of the defendant. Due process requires that a defendant be given adequate time to prepare before a proceeding in which his or her professional license may be revoked. See, *e.g.*, *Nell* v. *United States*, 450 F.2d 1090, 1093 (4th Cir. 1971) (holding that due process requires that an attorney's disbarment or suspension proceedings be preceded by an opportunity to prepare a defense). The right of an SEC respondent to adequately prepare his or her case is threatened by the arbitrary and unfair limitations imposed by the Rules of Practice. Due process is not served when the Division can conduct a lengthy and detailed investigation against an SEC respondent, but the respondent must then prepare his or her defense within (at most) ten months of the order instituting proceedings.

B. The Discovery Procedures and Practices in the Administrative Forum Deprive SEC Respondents of their Due Process Rights

The lack of meaningful discovery also deprives SEC respondents of constitutionally required procedural safeguards. "The right to present evidence is, of course, essential to the fair hearing required by the Due Process Clause." *Jenkins* v. *McKeithen*, 395 U.S. 411, 429 (1969). This Court has held in a criminal context that although "the Due Process Clause has little to say regarding the amount of discovery which the parties must be afforded * * * it does speak to the balance of forces between the accused and his accuser." *Wardius* v. *Oregon*, 412 U.S. 470, 474 (1973). To avoid running afoul of the Due Process Clause, "discovery must be a two-way street." *Id.* at 475. In examining state criminal discovery practices, for example, this Court has been "particularly suspicious of state trial rules which provide nonreciprocal benefits to the State when the lack of reciprocity interferes with the defendant's ability to secure a fair trial." *Id.* at 474 n.6. Indeed, this Court has stated that "the State's inherent information-gathering advantages suggest that if there is to be any imbalance in discovery rights, *it should work in the defendant's favor*." *Id.* at 475 n.9 (emphasis added). This parity is absent in SEC proceedings and is in contrast to such parity in Article III adjudications.

1. SEC Rules of Practice governing discovery favor SEC.

In a quasi-criminal proceeding like one before an ALJ, the restrictions that the Rules of Practice place on a discovery violate the due process rights of SEC respondents.

Although an SEC respondent in an administrative proceeding is entitled to the Division's investigatory file (see 17 C.F.R. 201.230(a)(1)), the respondent's ability to obtain discovery is otherwise significantly more restricted than the permissive discovery allowed under the Federal Rules of Civil Procedure. Nor does an SEC respondent benefit from discovery rights afforded in criminal proceedings under the Federal Rules of Criminal Procedure, the Jenks Act, 18 U.S.C. 3500, *Brady* v. *Maryland*, 373 U.S. 83 (1963), and *Giglio* v. *United States*, 405 U.S. 150 (1972).

Two-way discovery is not required in SEC proceedings. The Division has the power to subpoena documents and conduct examinations of potential SEC respondents and witnesses during an investigation, but SEC respondents have no corresponding ability to make demands of the Division. Similarly, the Division is able to subpoena sworn testimony over the course of the investigation. But, a respondent is permitted only a limited number of depositions, and only if an order instituting proceedings has been entered. It is precisely this type of "imbalance in discovery rights" that this Court has criticized as unfair. See *Wardius*, 412 U.S. at 475 n.9.

a. *Document Collection*

The Rules of Practice state that, if the Division recommends that the Commission institute an administrative proceeding, the SEC respondent is entitled to "any party documents obtained by the Division prior to the institution of proceedings, in connection with the investigation leading to the Division's recommendation to institute proceedings." 17 C.F.R. 201.230(a)(1). Although the SEC is accordingly required to provide an SEC respondent with all of its discovery, SEC respondent have no ability to take their own discovery to rebut whatever the SEC has provided. Therefore, SEC respondents are forced to, in essence, litigate against themselves using the evidence the Division has obtained in making out its case against the SEC respondent. The rejection of reciprocal discovery stands in significant contrast to the protections afforded by constitutionally adequate tribunals.

b. *Interrogatories and Requests for Admission*

The Division is similarly advantaged over SEC respondents by its ability to use interrogatories, requests for admission, and other written discovery to build its case, with no reciprocal rights for SEC respondents. There is no provision in the Rules of Practice that permits SEC respondents to request other documents, make requests for admissions, or propound interrogatories, as would be permitted in federal court. Compare 15 U.S.C. 77s(c), with Fed. R. Civ. P. 33 and 36. The inability to use these discovery tools deprives SEC respondents of the ability to gain valuable insight into the strengths and weaknesses of

the Division's case. SEC respondents lose the ability to narrow issues for trial and define the claims of the Division. Moreover, the inability of SEC respondents to use interrogatories prevents them from collecting evidence that might otherwise be available. *United States* v. *W. Virginia Pulp & Paper Co.*, 36 F.R.D. 250, 251 (S.D.N.Y. 1964) ("The obtaining of evidence, or even information which may lead to evidence, from an adverse party is one of the functions of interrogatories. A further function is to obtain admissions and narrow the issues to be tried."); *United States* v. *Purdome*, 30 F.R.D. 338, 340 (W.D. Mo. 1962) ("[I]nterrogatories serve two distinct purposes: First, to ascertain facts and to procure evidence, or secure information as to where pertinent evidence exists and can be obtained; second, to narrow the issues."'). Depriving SEC respondents of the ability to secure critical information in advance of trial and to reduce the number of issues that need to be addressed at trial make SEC respondents' nearly insurmountable odds even longer.

c. *Depositions*

Similarly, the Division may, through informal and formal investigations, take testimony, request documents, and examine a prospective SEC respondent (and respondent's employees) for years before administrative proceedings are instituted. The Division is permitted to take sworn subpoenaed testimony as part of its investigation and introduce such testimony as evidence. See *In Re Del Mar Fin. Servs., Inc.*, Release No. 8314 (Oct. 24, 2003) (holding that ALJ should have admitted investigative transcripts that "contained evidence that was relevant to the issues in the case"). Indeed, the Division has broad authority to subpoena witnesses and compel

production of documents as part of its formal investigatory process. See Section 19(c) of the Securities Act, Section 21(b) of the Securities Exchange Act, Section 209(b) of the Advisers Act, and Section 42(b) of the Investment Company Act.

Yet, SEC respondents' ability to take depositions is again conversely limited. In administrative proceedings operating under the 120-day timeframe pursuant to Rule 360(a)(2), SEC respondents may notice three depositions per side in single-respondent proceedings and may collectively notice five depositions per side in multiple-respondent proceedings. 17 C.F.R. 201.233(a)(1)-(2). A respondent or the Division may file a motion with the ALJ seeking leave to notice two additional depositions if the movant "demonstrates a compelling need" by, among other things, "[d]escribing * * * why the deposition of each witness and proposed additional witness is necessary for the moving side's arguments, claims, or defenses[.]" *Id.* at 201.233(a)(3).

SEC respondents or the Division may also notice additional depositions of witnesses if the ALJ or the Commission finds that the prospective witness will give material testimony, is unavailable, and that the taking of the deposition will serve the interests of justice. 17 C.F.R. 201.233(b). However, that provision has been interpreted narrowly by ALJs who frequently deny SEC respondents' requests for additional depositions. See, *e.g.*, *In re Delany*, Admin. Proceedings Rulings Release No. 1652, 109 SEC Docket 2282, 2014 WL 11115571 at *5 (July 25, 2014) (denying joint request pursuant to Rule 233(b) for subpoena despite witness having Parkinson's disease); *In re Daxor Corp.*, Admin. Proceedings

Rulings Release No. 666, 100 SEC Docket 1750, 2011 WL 7820430 at *3-4 (Feb. 24, 2011) (denying deposition for witness who was one of three doctors in specialty who worked at "short-staffed" hospital system despite "personal and professional hardship" and showing that testifying would be an "extreme burden" for the witness).

Critically, in 30-day and 75-day actions, SEC respondents are not permitted to notice depositions by right at all, and may notice depositions only of unavailable persons pursuant to Rule 233(b). See *id.* at 201.233(b). The reluctance of SEC ALJs to grant depositions under that provision potentially leaves SEC respondents in 30- and 75-day actions without the ability to notice depositions at all. Accordingly, although the Rules of Practice appear to award each side the same number of depositions, as a practical matter the Division has far greater ability to compel testimony, particularly in the 30- and 75-day contexts where the Division is permitted to take testimony as part of its investigation but SEC respondents are left without a corresponding right to notice depositions.

2. The Federal Rules of Civil Procedure level the playing field to ensure due process is preserved.

The strict limitations of the Rules of Practice stand in stark contrast to the liberal discovery standards set forth in the Federal Rules of Civil Procedure. See, *e.g.*, *Swierkiewicz* v. *Sorema N.A.*, 534 U.S. 512 (2002) ("This simplified notice pleading standard relies on liberal discovery rules and summary judgment motions to define disputed facts

and issues and to dispose of unmeritorious claims."); *Katz* v. *Batavia Marine & Sporting Supplies, Inc.*, 984 F.2d 422, 424 (Fed. Cir. 1993) ("It is a premise of modern litigation that the Federal Rules contemplate liberal discovery, in the interest of just and complete resolution of disputes.").

Were the Division to bring its actions in federal court, it would no longer have an overwhelming advantage with respect to fact gathering and discovery. It would be required to respond to requests for admission and interrogatories, and would have to respond to requests for relevant documents beyond the Division's investigatory file. SEC respondents in 30-day and 75-day proceedings would have the right to take depositions, a right that is now effectively denied to them. And, SEC respondents in 120-day proceedings would be guaranteed the full complement of ten depositions per party, at least double what SEC respondents would receive under the Rules of Practice. Full and fair liberal discovery is a "premise of modern litigation" and necessary for a fair resolution of disputes. The Commission's extreme limits on discovery rights deprives SEC respondents of the ability of fully and fairly defend themselves in quasi-criminal proceedings before an ALJ and violates their due process rights.

C. The Evidentiary Rules in the Administrative Forum Deprive SEC Respondents of their Due Process Rights

In addition to the lack of parity in information-gathering powers between the Division and SEC respondents, the Rules of Practice give the Division wide latitude to use evidence against SEC respondents that would not be admissible in an Article III court. The permissive admissibility standard in the administrative forum favors the Division and allows convictions of SEC respondents for securities law violations based upon inadmissible evidence. A practice whereby hearsay or other ordinarily inadmissible evidence can be used to impose quasi-criminal penalties on SEC respondents is inconsistent with the principles of due process.

The Federal Rules of Evidence do not apply in administrative hearings before an SEC ALJ. An ALJ may receive any relevant evidence, and need only exclude evidence that is "irrelevant, immaterial, unduly repetitious, or unreliable." 17 C.F.R. 201.320(a). ALJs may admit all evidence that "can conceivably throw any light upon the controversy." *In re Jesse Rosenblum*, 47 SEC 1065, 1072 (1984). Even hearsay is admissible. *In re Leslie A. Arouh*, 99 SEC Docket 32306, 32323 (Sept. 13, 2010), see also *In re Del Mar Fin. Servs., Inc.*, Release No. 8314 (Oct. 24, 2003) ("We have stated on numerous occasions that the Federal Rules of Evidence, including the rules on hearsay, are not applicable to our administrative proceedings which favor liberality in the admission of evidence.").

As discussed above, the Division often seeks sanctions, including excessive monetary penalties or an industry bar, which are tantamount to criminal penalties. It is only fair that an SEC respondent is afforded the full panoply of procedural protections in a proceeding in which a government actor is seeking to deprive the respondent of his or her livelihood. The Federal Rules of Evidence serve an important gatekeeping function that protects defendants in federal court. *Daubert* v. *Merrell Dow Pharma.*, 509 U.S. 579, 587 (1993) ("That, nevertheless is the balance that is struck by the Rules of Evidence designed not for the exhaustive search for cosmic understanding but for the particularized resolution of legal disputes."). The rules have been carefully crafted by Congress to balance the interests of full disclosure of the relevant facts with the need to ensure reliability. By admitting hearsay evidence and otherwise disregarding federal evidentiary rules, the Rules of Practice disturb this carefully crafted balance and expose SEC respondents to quasi-criminal penalties without the full protection they deserve.

D. The Structure of the Administrative Hearing Deprives SEC Respondents of their Due Process Rights

SEC ALJs lack independence. They are part of the same administrative agency that is conducting the prosecution, making the regulations, and interpreting the applicable law. SEC respondents thus are forced to submit to an administrative hearing before an executive officer who decides their guilt or innocence, and imposes sanctions that can cripple livelihoods. This forum, in which the executive and adjudicative functions are performed by the same agency, does not

allow for a fair and impartial trial before an independent arbiter. See *Lawson*, 107 Harv. L. Rev. at 1248 ("The destruction of th[e] principle of separation of powers is perhaps the crowning jewel of the modern administrative revolution. Administrative agencies routinely combine all three governmental functions in the same body, and even the same people within that body."). SEC ALJs rarely exercise independence from the SEC in a way that safeguards the due process rights of SEC respondents. The partiality of the ALJs and their ability to control the administrative proceedings leaves many SEC respondents with little choice but to accept a settlement and admission of liability. The procedural hurdles discussed above combine with the SEC's built-in home court advantage to create an administrative forum in which a respondent is almost certain to be found liable. Indeed, over a five-year period from 2010 to 2015, the SEC won 95 percent of its administrative proceedings.[2]

The structural disadvantages continue throughout the proceedings. At no point over the course of an administrative hearing does an SEC respondent have an ability to develop a full and fair record before an Article III fact finder. From the outset of an investigation through the administrative proceedings, a respondent's ability to shape the record and collect evidence is limited. Even if the SEC respondent appeals to a federal court of appeals the procedural disadvantages continue to haunt them, as they are reliant on the limited discovery permitted and

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[2] See Jean Eaglesham, *SEC Wins With In-House Judges*, WALL ST. J. (May 6, 2015), http://www.wsj.com/articles/sec-wins-with-in-house-judges-1430965803.

evidence adduced in the administrative context to form the record for appeal.

II. The Lack of Meaningful Judicial Review of an ALJ Decision Deprives SEC Respondents of Their Due Process Rights

Should SEC respondents proceed through a hearing, procedural biases are rarely cured by a Commission that too frequently rubber stamps the outcomes of the hearings below. The Commission's determination is then subject to only limited federal review that is constrained by the record developed before the ALJ.

Although SEC respondents have a right to appeal the determination of an ALJ to the full Commission, *de novo* review by the Commission is anything but independent. See 17 C.F.R. 201.410. From 2010 to 2015, the Division won 88 percent of its appeals of ALJ decisions.[3] Such an overwhelming success rate is to be expected given the built-in procedural and evidentiary advantages the Division enjoys before the ALJ. The ALJ's ability to shape the record and the Commission's rubber stamping of the ALJs' determinations, creates a forum in which fair adjudication is rare, if not impossible.

A respondent's path gets no easier if he or she elects to take the case to a federal court of appeals. The ALJ is afforded significant deference on both factual and legal determinations. A court of appeals will review questions of fact decided by the ALJ under a "substantial evidence" standard. See *Universal*

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[3] *Ibid.*

Camera Corp. v. *NLRB*, 340 U.S. 474, 477 (1951). Legal determinations are accorded *Chevron* deference, which requires the court to defer to the SEC's reasonable interpretation of its own organic statute. See *Chevron, U.S.A., Inc.* v. *Nat. Res. Def. Council*, 467 U.S. 837, 844 (1984). A respondent's burden is even greater given the procedural inequities present at the administrative hearing. Because the federal appellate court is not empowered to take testimony, a respondent is limited to the record created before the SEC. Accordingly, judicial review by a court of appeals does not provide a sufficient remedy for the inequities inherent in the Commission's Rules of Practice.

III. SEC Enforcement Proceedings' Constitutional Infirmities Are Compounded Because ALJs Are Not Appointed Pursuant to the Appointments Clause

As explained above, SEC enforcement proceedings lack many of the hallmarks of due process protections provided in federal district court litigation.

These constitutional failings are exacerbated because the ALJs themselves are merely agency employees, not subject to the Appointments Clause. Such appointment would provide the imprimatur of the executive branch on SEC administrative proceedings before ALJs, because the ALJs would be answerable to the President. It is critical to the protection of SEC respondents' due process rights that ALJs be constitutionally appointed so that they are ultimately answerable to the will of the American people. The Appointments Clause is critical to

preserving that political accountability and thereby "the Constitution's structural integrity." See *Freytag*, 501 U.S. at 878, 884. ALJs wield great power in SEC proceedings—proceedings that are already rife with disparities between the SEC and SEC respondents. ALJs make critical evidentiary decisions over how the record is created and also provide legal interpretations of the statutory schemes. ALJs also, at the end of proceedings, levy individual sanctions that can prohibit individuals from working in any regulated financial service industry. Given the lack of constitutionally adequate safeguards that already permeate SEC proceedings, it is a bare minimum of due process protections for the person presiding over such proceedings to be appointed by the President and, ultimately, answerable to the President. That step is critical to ensuring constitutionally adequate due process protections.

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The SEC has broad power to impose devastating penalties on companies and individuals. As this Court has remarked, the government "is not only a different kind of plaintiff, it seeks a different kind of relief." *Gabelli*, 568 U.S. at 451. The SEC has the ability to bar individuals from the securities industry and impose crippling punitive fines. These quasi-criminal penalties underscore the need to ensure that the due process rights of every respondent that practices before the SEC are protected. The Appointments Clause provides one such guarantee.

CONCLUSION

The judgment of the United States Court of Appeals for the District of Columbia Circuit should be reversed.

Respectfully submitted.

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